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Public Policy and Saving for Retirement: The “Autosave” Features of the Pension Protection Act of 2006

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On August 17, 2006, President Bush signed the Pension Protection Act of 2006 (PPA) into law, following its passage by both houses of Congress in a strong showing of bipartisan support.¹ This law, probably the most sweeping piece of pension reform legislation since the Employee Retirement Income and Security Act of 1974 (ERISA), contains many different pension reform provisions.² In this paper, we focus on a subset of measures within the PPA adopted specifically to promote better savings outcomes in defined contribution savings plans.

The push for these provisions came in response to a growing body of economic research showing first, that many individuals are not saving enough for retirement (despite a stated desire to save more), and second, that many individuals are largely passive in their retirement savings behavior. The “autosave” features encouraged in the Pension Protection Act aim to harness the power of inertia to increase employee savings—if employees do nothing, the result will be that they are saving rather than that they are not.

This paper first summarizes the autosave features of the PPA, then describes the economic research that motivates them, and finally discusses how this research was translated into policy.

The Autosave Features of the Pension Protection Act

The Pension Protection Act promotes employer adoption of some or all of the following “autosave” features in their defined contribution savings plans:

- Automatic enrollment—employees are automatically enrolled in the savings plan at a default contribution rate and default asset allocation unless they explicitly choose to opt out.
- Employer contribution—the employer makes a contribution to employee accounts, either on a non-contingent basis (independent of whether employees contribute anything) or as a match on employee contributions.
- Contribution escalation—participant contributions to the savings plan automatically increase over time.
- Qualified default investment alternative (QDIA)—contributions are defaulted into a diversified portfolio that includes exposure to both equity and fixed income assets.

The encouragement for employers to incorporate these features into their savings plans comes in several different forms. Although many employers recognized the potential benefit to employees of autopilot savings plans well before the PPA, some were reticent to adopt these features because of various legal concerns. PPA eliminated the legal underbrush on which many employer objections had rested.

One such legal issue was an employer’s potential liability for investment losses in the default fund under automatic enrollment. ERISA (section 404(c)) affords employers relief from legal liability for losses resulting when participants in employer-sponsored savings plans direct

¹ The bill was passed by the Senate in a 93-5 vote and by the House of Representatives in a 279-131 vote.

² See the U.S. Department of Labor’s pension reform website for more details on the Pension Protection Act (including the complete text of the 393-page act): <http://www.dol.gov/EBSA/pensionreform.html>.

the asset allocation of their investments themselves. PPA extends this protection to default investments under automatic enrollment (and in other circumstances when participants fail to make an explicit asset allocation election) if these defaults satisfy certain requirements, including exposure to more than one asset class.³

Finally, plans that adopt automatic enrollment with automatic contribution escalation⁴ and a sufficiently generous employer contribution⁵ are exempted from annual non-discrimination testing. The non-discrimination tests are regulations designed to ensure that the tax benefits of savings plan participation do not accrue disproportionately to “highly compensated” employees. To pass the non-discrimination tests, firms must demonstrate that the participation and savings rates of employees with compensation below the “highly compensated” income limit are sufficiently high relative to employees whose incomes are above the threshold.⁶ Demonstrating compliance is costly to employers, and there are additional costs associated with restructuring savings plans to achieve compliance in the event that a firm would not otherwise pass. If employers adopt conforming autosave features, they are exempt from having to demonstrate compliance. More generally, the exemption sends a signal to firms about what the Internal Revenue Service (IRS) and the Department of Labor (DOL), which jointly regulate employee benefit plans, deem to be acceptable and encouraged plan design features.

The Economic Research Behind the Autosave Features of the Pension Protection Act

Understanding the significance of these Pension Protection Act provisions requires some historical context. Until the 1970s, most employers who provided retirement income benefits for their workers did so using traditional defined benefit pension plans. In 1975, there were 2.4 participants in defined benefit pension plans for every one participant in a defined contribution plan (Department of Labor, 2007). In the 1980s, however, the pension landscape began to change, precipitated by a series of new laws and regulations starting with the 1974 passage of ERISA. This act made it more costly for employers to offer traditional defined benefit pension plans to their workers. ERISA was followed by the addition of section 401(k) to the Internal Revenue Code in 1978. In 1981, an IRS clarification of the definition of taxable income allowed employers to exempt contributions to 401(k) savings plans from taxable income.

Although the 1978 legislation and the 1981 clarification were not intended to transform the U.S. pension landscape, this is in fact what ensued. Section 401(k) gave firms a tax-favored option for providing retirement income benefits at a lower regulatory cost than that of traditional

³ These Qualified Default Investment Alternative (QDIA) regulations specifically endorse three different long-term investment options: life cycle or target retirement date funds, balanced funds, and professionally managed accounts (see <http://www.dol.gov/ebsa/pdf/fsQDIA.pdf> and <http://www.dol.gov/ebsa/regs/fedreg/final/07-5147.pdf>).

⁴ The default contribution rate must be 3% or higher initially, and then escalate by 1% each year until reaching a rate of at least 6% and no more than 10%. Contribution escalation can presumably continue beyond the 10% level with a participant’s affirmative election.

⁵ Employers can choose either a non-contingent contribution of 3% of pay for all employees (regardless of whether the employees choose to contribute themselves) or an employer match of 100% on the first 1% of pay contributed to the plan and 50% on further contributions up to 6% of pay (for a total matching contribution of 3.5% of pay if employees contribute at least 6% of their pay to the plan). A more generous non-contingent contribution or employer match is also acceptable.

⁶ The income threshold for classification as a “highly compensated employee” has increased over time, and is set at \$105,000 for 2008.

defined benefit pensions in the post-ERISA environment. The 401(k) plan, originally intended as a supplemental savings vehicle, caused a complete upheaval of the employer-provided pension plan system. By the mid-1980s, both the number of defined benefit pension plans and the number of participants in these plans had started a steady (and ongoing) decline. Defined contribution savings plans—principally the 401(k) and its close cousins, the 403(b) and 457 plans—filled the breach. In 2004, the latest year for which data are available, defined contribution participants outnumbered defined benefit participants by a ratio of 2.5 to one, a complete reversal of the situation thirty years earlier (Department of Labor, 2007).

Employers initially adopted a “Field of Dreams” approach to defined contribution savings plans in this new era: if we offer it, they will save. The initial philosophy was that individuals know what savings outcomes are in their best interest and will achieve these outcomes through their savings plan choices. The hallmark of this first generation of defined contribution savings plans was choice: individuals choose whether or not to participate, how much to save, and how to allocate their assets.

The foundations underlying this presumption began to crumble as research uncovered how poorly employees were actually utilizing defined contribution savings plans. In a series of surveys conducted periodically from 1991 to 2004, John Hancock Financial Services documented a striking lack of financial knowledge among defined contribution plan participants. In the most recent published version of the survey, 38% of respondents claimed that they had little or no investment knowledge, and two-thirds reported that they would be better off working with a financial advisor than managing their retirement investments on their own (John Hancock Financial Services, 2002). This self-perceived lack of expertise is corroborated by more objective measures of financial knowledge (Choi, Laibson, and Madrian, 2007; Lusardi and Mitchell, 2006).

Financial ignorance need not be a problem if individuals can obtain reliable advice from those who are more knowledgeable, and then expeditiously implement that advice. In the age of defined benefit pension plans, employers filled the role of a (paternalistic) retirement savings advisor. Employers performed the complicated calculations required to determine how much money to set aside today to achieve the wealth needed to maintain consumption in retirement; employers contributed this amount to the pension plan without any active intervention by employees; and employers were responsible for managing the pension asset allocation. All of these tasks were done with the help of financial professionals. But in the transition from defined benefit to defined contribution savings plans, many employers stepped out of this paternalistic role.

Strong evidence of the poor personal financial management that ensued comes from research on savings outcomes under automatic enrollment (Madrian and Shea, 2001; Choi, Laibson, Madrian, and Metrick, 2002, 2004 and 2006; Beshears, Choi, Laibson, and Madrian, 2008). Most defined contribution savings plans have historically required employees to proactively enroll in order to initiate participation. As part of the enrollment process, employees choose a contribution rate and an asset allocation. In contrast, under automatic enrollment, employees are enrolled in the plan at a contribution rate and asset allocation pre-specified by the employer unless they either explicitly opt out of participation or choose a different contribution

rate and/or asset allocation. Automatic enrollment does not alter the set of options available to employees. It simply replaces one default (non-participation) with another (participation at a particular contribution rate and asset allocation). But this seemingly small procedural change generates significant differences in savings outcomes.

Figure 1 shows the relationship between employee tenure (the x -axis) and savings plan participation rates (the y -axis) at a large chemicals firm for three groups of employees: those hired before automatic enrollment was introduced, those hired under automatic enrollment with a default contribution rate of 3% of pay, and those hired under automatic enrollment with a default contribution rate of 6% of pay. There is a large difference in participation rates between those hired before and those hired after automatic enrollment. Participation rates prior to automatic enrollment start below 50% for newly hired employees and gradually increase to about 75% for those with more than two years of tenure. In contrast, participation rates for employees hired after automatic enrollment exceed 90% once employees who do not opt out have been swept into the savings plan in their third month of employment. The participation rate under automatic enrollment does not appear to depend on whether the default contribution rate is 3% or 6%.

These differences are particularly surprising given the low costs of implementing a change in participation status. In survey responses, employees who have signed up for their employer's savings plan report that doing so took about an hour and a half; employees who have not signed up estimate that it would take them a similar amount of time (Choi, Laibson, and Madrian, 2007). These time costs are modest compared to the substantial financial consequences of participation, the largest of which is the employer matching contribution (for example, the company in Figure 1 offers a dollar-for-dollar match on employee contributions up to 6% of pay). Other benefits include favorable tax treatment and higher future consumption (which must be weighed against the cost of decreased current consumption).

It is not clear which of the tenure-participation profiles in Figure 1 most closely reflects the true savings preferences of employees. Other evidence, however, leads us to the conclusion that most employees prefer to be saving early in their tenure. First, the opt-out rate under automatic enrollment is low (Madrian and Shea, 2001; Choi, Laibson, Madrian, and Metrick, 2002 and 2006). Most of those who opt out do so almost immediately; few employees who are automatically enrolled later decide that they would rather not be contributing to the savings plan. In contrast, when the default is non-participation, the rate at which employees opt into savings plan participation is initially high and persistently positive, even after several years. Second, when employees are required to make an active "in-or-out" savings plan participation decision around 70% of employees choose to join the plan (Carroll et al., 2007). In addition, when asked, most employees state a preference to save more than they currently are (Choi, Laibson, Madrian, and Metrick, 2002 and 2006; Thaler and Benartzi, 2004; Bernheim, 1995; Farkas and Johnson, 1997). Finally, a 2007 Harris Interactive poll finds that 98% of plan participants who were enrolled under automatic enrollment and did not opt out agree with the statement that "You are glad your company offers automatic enrollment." More surprisingly, 79% of the employees who *did* opt out of the savings plan also agree. These various pieces of evidence suggest that most employees prefer to be participating in their employer-sponsored savings plan and that automatic enrollment is a useful mechanism for expediting enrollment. Hence, there is a strong rationale for encouraging employer adoption of automatic enrollment through the Pension Protection Act.

Automatic enrollment affects not only participation status, but also contribution rates and asset allocation. Figure 2 shows the distribution of contribution rates for participants at a large food company before automatic enrollment, under automatic enrollment with a 3% default contribution rate, and under automatic enrollment with a 4% default contribution rate.⁷ Like the company shown in Figure 1, this company provides a match on employee contributions up to 6% of pay. Before automatic enrollment, 84% of participants elected to contribute at or above the 6% match threshold, and very few had a contribution rate of 3% or 4%. Automatic enrollment dramatically shifts the distribution of contribution rates. When the default contribution rate is 3%, almost half of participants have a 3% contribution rate; when the default contribution rate is 4%, almost half have a 4% contribution rate. Under both automatic enrollment regimes, less than half of participants contribute at or above the match threshold—substantially fewer than the 84% at or above the threshold before automatic enrollment. The distribution of asset allocations, not shown in Figure 1, exhibits a similarly large shift towards the default asset allocation.

The default effect is not only large initially, but it persists for a long time. Figure 3 shows the relationship between tenure and the probability of retaining both the default asset allocation and default contribution rate at four companies with automatic enrollment. The fraction of participants at these defaults is initially very high but declines with tenure as participants begin to elect their own contribution rates and asset allocations. Despite this decline, a large fraction of participants remains at the default even at high levels of tenure (e.g. over three years). Although not shown in Figure 3, the default asset allocation is slightly more persistent than the default contribution rate.

Figure 3 understates the persistence of the default asset allocation in one important dimension. Even when automatically enrolled participants trade out of the default fund, their new asset allocation tends to be closer to the default than the asset allocations chosen by participants who were hired before automatic enrollment (Madrian and Shea, 2001; Beshears, Choi, Laibson, and Madrian, 2008). The reason for this persistence may be that employees perceive the default as having been implicitly endorsed by the employer. This endorsement effect also appears after a company adopts automatic enrollment, in the form of higher allocations to the default fund among participants who were not themselves subject to automatic enrollment (because they were hired before automatic enrollment was implemented).⁸

Of course, the outcome that matters most is asset accumulation, which depends on all of the variables discussed above: participation, contribution rates, and asset allocation. On this front, automatic enrollment can be a two-edged sword. Automatic enrollment clearly increases asset accumulation (at least within the savings plan) for employees who would not have participated otherwise. But how does it affect asset accumulation for employees who would have

⁷ Because of concurrent 401(k) eligibility changes for employees under the age of 40 at this company, we restrict the analysis to employees aged 40 or over at the time of hire. These employees were immediately eligible to participate in the 401(k) plan both before and after the switch to automatic enrollment.

⁸ A similar endorsement effect may influence employee allocations to employer stock, which are higher in firms that direct the employer match into employer stock than in firms where employer stock is simply available as an investment option (Benartzi, 2001; Brown, Liang, and Weisbenner, 2007).

participated anyway? The answer to this question hinges critically on how the default compares to what employees would have chosen in the absence of automatic enrollment.

Choi, Laibson, Madrian, and Metrick (2004) show that for some employees who would have participated in the absence of automatic enrollment, there is no effect on asset accumulation: these employees opt out of the automatic enrollment defaults early on and choose the same contribution rate and asset allocation that they would have chosen without automatic enrollment. But other employees are heavily influenced by the automatic enrollment defaults. Automatic enrollment raises the contribution rates of the left tail of the savings distribution; those who would save nothing are induced to participate. But in the absence of automatic enrollment, many employees would have eventually enrolled at a contribution rate that is at or above the match threshold, with an asset allocation that is likely to contain substantial equity exposure. If the default contribution rate is below what employees would have chosen without automatic enrollment, and if the default asset allocation has a lower expected return than the asset allocation that employees would have chosen on their own, then the resulting low contribution rates and expected asset returns may outweigh the acceleration of participation under automatic enrollment, depressing the rate of asset accumulation.⁹ In the long term, these employees may actually be worse off as a result of automatic enrollment.

Whether automatic enrollment reduces asset accumulation depends on the defaults adopted by employers. Many employers have historically chosen defaults—low contribution rates and conservative default funds—that could work against long-run asset accumulation. This possibility provides the rationale for two of the other key autosave components of PPA: the adoption of contribution escalation as part of the non-discrimination testing safe harbor, and the qualified default investment alternative (QDIA) guidelines.

Although the PPA non-discrimination testing exemption allows for a fixed default contribution rate of 6% or higher, the baseline specified in the legislation is automatic enrollment with a lower initial default contribution rate of 3% in conjunction with contribution escalation—specifically, automatic annual contribution rate increases of 1% continuing until participants have reached at least a 6% contribution rate, but no more than a 10% contribution rate.

Thaler and Benartzi (2004) document the effectiveness of contribution escalation at increasing employee savings rates. At the firm they study, employees who opted into an automatic annual 3 percentage point contribution increase saw their average contribution rate increase almost four-fold over the course of four years, from 3.5% of pay to 13.5% of pay. In contrast, employees who did not elect contribution escalation increased their average contribution rate by much less over the same time period, from 5.3% to 7.5%. Interestingly, the latter group started out saving much more than those who opted into contribution escalation, but their relative positions were reversed four years later. As might be expected given the evidence on automatic enrollment, contribution escalation is much more effective if it is the default, harnessing employee inertia to increase contribution rates. In firms where contribution escalation is an option but is not the default, about 25% of savings plan participants sign up; in contrast,

⁹ Of course, lower expected asset returns may be acceptable or even desirable if they are associated with less risk. However, standard economic theory suggests that individuals should be willing to accept at least some stock market risk, so that some exposure to the higher expected return of equities is attractive from a normative standpoint.

when contribution escalation is the default, only 15% of participants opt out, so that 85% of participants are subject to future automatic contribution increases (Benartzi, Peleg, and Thaler, 2007).

Combining automatic enrollment with contribution escalation mitigates the drag on long-term asset accumulation that results under automatic enrollment with a low default contribution rate. However, picking a higher initial default contribution rate is also an option (with or without contribution escalation). Relative to the PPA benchmark (3% initial contribution rate with contribution escalation), picking a higher initial contribution rate with contribution escalation will lead to the greatest level of asset accumulation, provided that it does not result in significantly higher opt-out rates. Picking a higher initial contribution rate without contribution escalation will lead to higher asset accumulation than the PPA baseline in the short run, but may result in lower asset accumulation in the long run.

As with contribution escalation, the qualified default investment alternative (QDIA) guidelines also mitigate the potential drag on long-term asset accumulation under automatic enrollment. In this case, the pertinent issue is the lower expected investment returns that accompany a conservative default fund. The rationale employers have given for selecting such conservative defaults has been a desire to forestall participant lawsuits if the default fund declines in value; by choosing a default fund designed to preserve principal, this risk is minimized (if not eliminated). PPA diminishes this rationale by shielding plan sponsors from legal liability if the default fund they choose satisfies certain conditions, including diversification (which precludes using a single asset, such as employer stock, as a QDIA default) and exposure to both equity and fixed income assets.

Moving from Research to Policy

The discussion above describes the evidence behind and rationale for the autosave and QDIA regulations that are part of PPA. Another important part of the story, however, is how the provisions came to be actually incorporated into law.

McDonald's is commonly cited as the first company to have incorporated automatic enrollment in its 401(k) plan, starting in 1984.¹⁰ By the mid-1990s, a handful of other companies had also adopted automatic enrollment. The oft-cited motivation for doing so was to increase participation rates among lower-paid employees so that the firm's savings plan would pass the non-discrimination tests and maintain its tax-qualified status. There were some questions, however, about the permissibility of automatic enrollment. Could employers legally direct employee contributions to an employer-sponsored savings plan without the affirmative consent of employees, and could the absence of a "negative election" (that is, opting out) under automatic enrollment be construed as approval to make such contributions?

In 1997, a curious Treasury Department staffer requested an IRS decision on the permissibility of 401(k) automatic enrollment. The staffer's request was initially denied; investing scarce resources for the legal comfort of a few companies that had not formally

¹⁰ Interestingly, McDonald's abandoned automatic enrollment in 2002, just as it was gaining popularity among other employers.

requested such a decision did not appear warranted. But further reflection led Mark Iwry, the Benefits Tax Counsel at the Treasury Department, to recognize that automatic enrollment had the potential to increase savings and improve retirement security for millions of Americans. An affirmative ruling on the permissibility of automatic enrollment might lead to more widespread adoption. So in 1998, Treasury/IRS issued Revenue Ruling 98-30, which described an acceptable scenario for 401(k) automatic enrollment.

In contrast to private rulings, which are issued in response to directed questions by private parties, revenue rulings are more general. The scenario in Ruling 98-30 involved a hypothetical company using automatic enrollment with a 3% default contribution rate invested in a balanced fund and an employer match that was not directed into employer stock. These seemingly ancillary details about the employer match were chosen quite purposefully. Mark Iwry and the staff at Treasury had two concerns about automatic enrollment. First, they were worried that firms might substitute automatic enrollment for an employer match as a way to satisfy the non-discrimination rules, a move that could nullify or even reverse the savings increases that might otherwise occur under automatic enrollment. Second, they were worried that employers might use automatic enrollment to funnel 401(k) contributions into employer stock in order to inflate its price. For firms interested in implementing automatic enrollment with the blessing of the IRS, the safest course of action would be to emulate the ruling's example precisely—that is, with the provision of an employer match that was not directed into employer stock.

This initial ruling was followed by a June 1998 speech by President Bill Clinton in which he endorsed automatic enrollment as a mechanism for increasing savings; then Treasury Secretary Lawrence Summers also encouraged employer adoption of automatic enrollment in some of his public remarks. Despite a belief within Treasury that automatic enrollment should be heavily endorsed, there were concerns that moving too quickly could backfire politically. Automatic enrollment could be perceived as being overtly paternalistic or yet another burdensome employer obligation. Either of these outcomes could result in Congressional action to block 401(k) automatic enrollment programs. Thus, Treasury/IRS began issuing a series of successively more expansive rulings meant to illustrate the different types of plans and automatic enrollment schemes deemed acceptable. The hope was that this gradual expansion would nudge employers toward automatic enrollment schemes with desirable features without stirring up too much political controversy.

These actions by Treasury coincided with the emergence of the first research findings on how automatic enrollment and contribution escalation affect savings outcomes. Although Treasury officials had worried about automatic enrollment displacing employer matches and being used to direct savings plan assets into employer stock, neither of these fears seemed to have been realized in practice. The biggest drawback to automatic enrollment was one that had not been anticipated: the persistence of the default options chosen by employers. As discussed previously, low default contribution rates reduce the contribution rates of individuals in the right tail of the savings distribution, and individuals do not quickly move away from these low defaults. Thus, 401(k) automatic enrollment could have a neutral or even negative net effect on aggregate retirement asset accumulation. Similarly, if employers adopted conservative default funds with expected returns below that of the assets employees would otherwise choose for themselves, account balances would grow more slowly in expectation.

Although all the revenue rulings issued by IRS/Treasury used a balanced fund as the default investment option, most early adopters of automatic enrollment opted for much more conservative money market or stable value default funds. Employers were concerned that a default fund which declined in value could give rise to a participant class-action lawsuit. Treasury could do little more on this front given that its existing revenue rulings already specified more aggressive defaults (balanced funds). But Treasury could encourage higher initial default contribution rates and contribution escalation. One of the revenue rulings in 2000 specified a 4% default contribution rate, in contrast to the 3% default rate specified in earlier rulings. This was followed in 2004 by an IRS general information letter¹¹ which clarified that employers have substantial discretion in structuring default contributions under automatic enrollment, including default contribution rates that are higher (or lower) than those used in previous revenue rulings, default contribution rates that are higher (or lower) than the employer match threshold, and default contribution rates that increase over time—that is, automatic contribution escalation.

As the results of the academic research began to diffuse, automatic enrollment and contribution escalation gained traction with employers, savings plan administrators, and benefits consultants. The staunchest opponents were those who felt that automatic enrollment and contribution escalation were too paternalistic. But these concerns were largely allayed by the argument that with or without automatic enrollment and contribution escalation, a company savings plan has a default; the question is simply what that default should be.

The discomfort some employers felt in adopting automatic enrollment was not entirely philosophical. There were several legal issues that made many employers reluctant to adopt so-called autopilot savings plans. Some did not feel adequately shielded from state laws that prohibit employers from withholding money from an employee's paycheck without consent. Other companies were concerned about potential legal liability associated with choosing a default fund that would likely hold a significant fraction of the plan's assets going forward. Still others were concerned about the tax implications of automatic enrollment for employees who did not want to participate in the savings plan but who did not opt out of participation before the opt-out deadline. These employees would incur a 10% tax penalty if they tried to recover the contributions they had made inadvertently. Congressional action was required to address these concerns.

Peter Orszag and Mark Iwry of The Retirement Security Project took the lead in incorporating into the Pension Protection Act provisions that would encourage employers to adopt automatic enrollment and contribution escalation (including clearing out the legal underbrush mentioned above) and in pushing the legislation through Congress. They were helped by groups such as the Profit Sharing/401(k) Council of America (representing the interests of employers), AARP (representing the interests of older individuals), and the non-partisan Employee Benefit Research Institute. The sell was not a difficult one; most of the key political constituencies were quickly convinced that automatic enrollment was aligned with their own interests. Employee support for automatic enrollment was widespread, leading to the backing of

¹¹ A general information letter is a device used by the IRS when a ruling does not seem necessary because a point is sufficiently obvious but may require clarification.

labor unions.¹² Employers were generally in favor; the proposed legislation would grant relief from legal liability for investment losses in qualifying default funds, and it would also grant relief from non-discrimination testing to employers that adopted sufficiently generous forms of automatic enrollment. Employers were also not required to adopt automatic enrollment if they did not want to. The financial sector recognized that automatic enrollment and contribution escalation would increase assets that they would manage. The failure of Social Security reform spurred an interest in promoting increased private savings among both conservatives and liberals, and although liberals were generally more inclined to support strengthening traditional defined benefit pension schemes, they were swayed by the evidence that automatic enrollment had the largest beneficial impact on the savings outcomes of lower-income individuals and minority groups. In the words of Peter Orszag, automatic enrollment “had become like apple pie on Capitol Hill—everyone was for it.”¹³

Orszag attributes the success of the autosave features in the Pension Protection Act to three factors.¹⁴ First, there was clear and compelling evidence that automatic enrollment was an effective means of increasing savings and improving economic wellbeing, particularly of minorities and of the poor. The evidence and the theory behind automatic enrollment and contribution escalation were transparent and convincing. Second, the results of the economic research on the isolated adoption of automatic enrollment and contribution escalation were clearly scalable and conformed to intuition and to experience. Third, as noted above, the effects of automatic enrollment appealed to both sides of the political aisle.

The U.S. is not the only country to recognize the impact that automatic enrollment can have on savings outcomes. In New Zealand, the KiwiSaver Act adopted in 2006 creates a new national program based on automatic enrollment to supplement the existing superannuation scheme. On the other side of the Atlantic, the United Kingdom’s Pensions Act of 2007 also incorporates automatic enrollment as part of its pension system reforms. Although it is too early to determine the efficacy of these programs, widespread take-up of 401(k) automatic enrollment in the United States is encouraging, inspiring Orszag to declare the autosave features of the Pension Protection Act “a stunning example of the success of behavioral economics in affecting public policy.”¹⁵

¹² See Harris Interactive (2007) for evidence on widespread employee support of automatic enrollment.

¹³ Interview with Peter Orszag, July 3, 2007.

¹⁴ Ibid.

¹⁵ Ibid.

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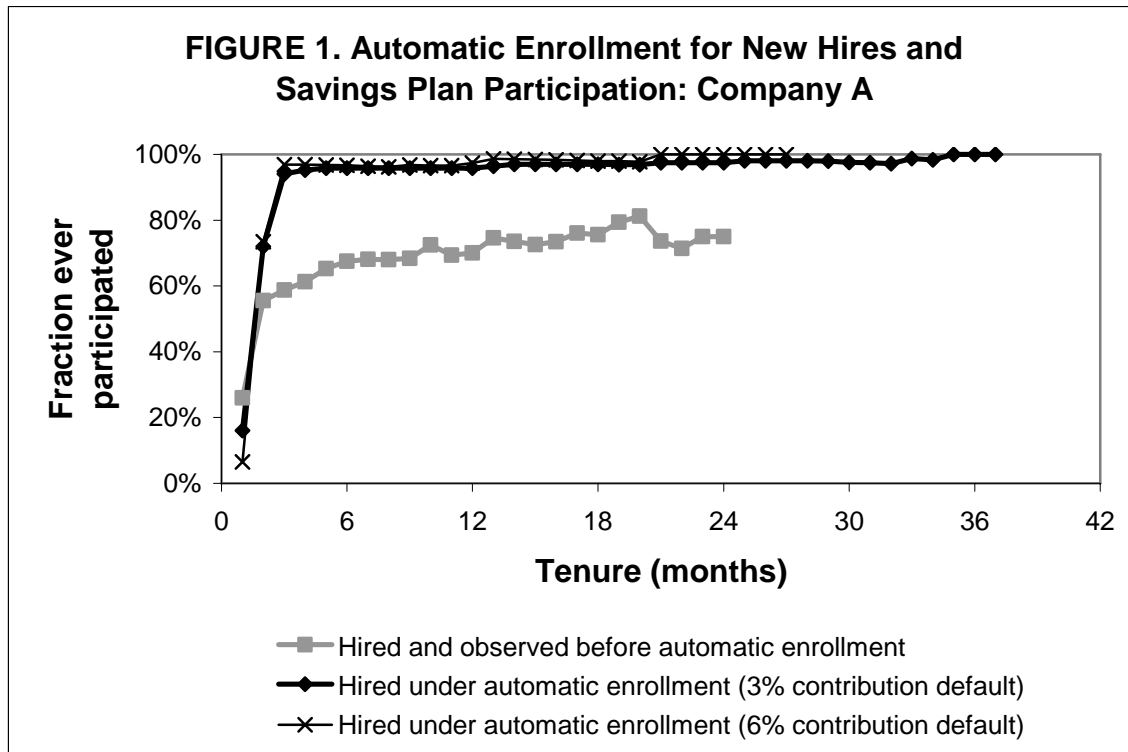
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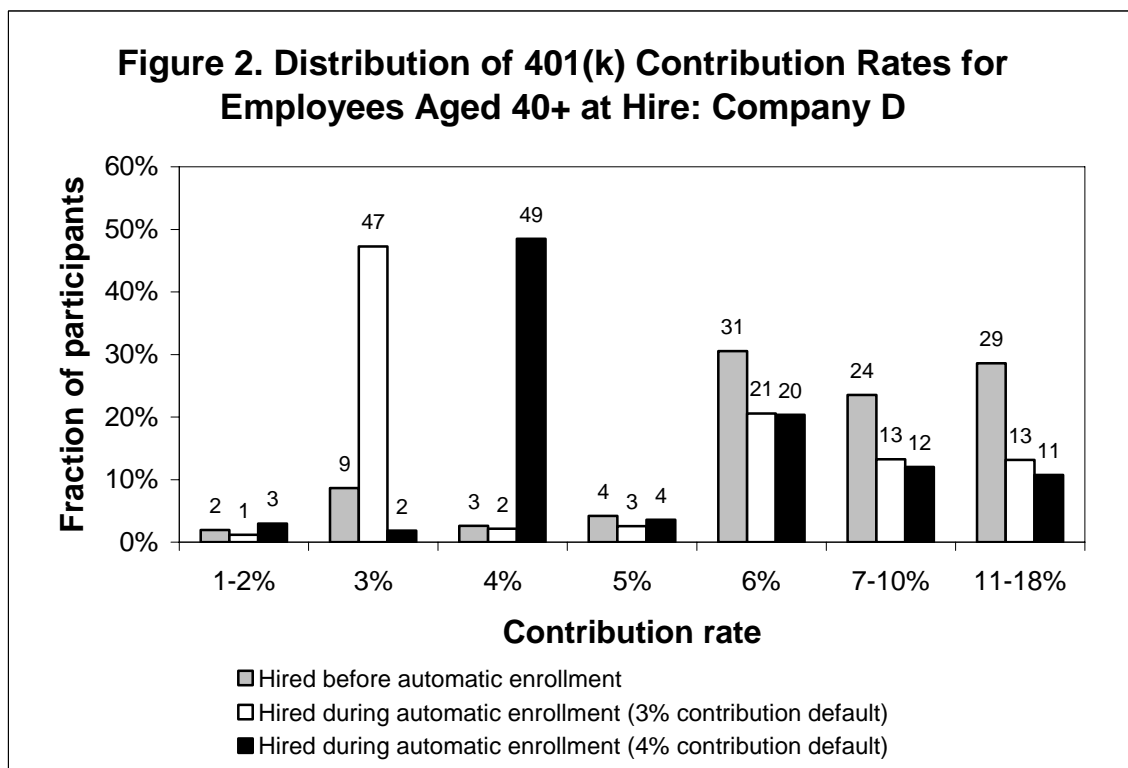
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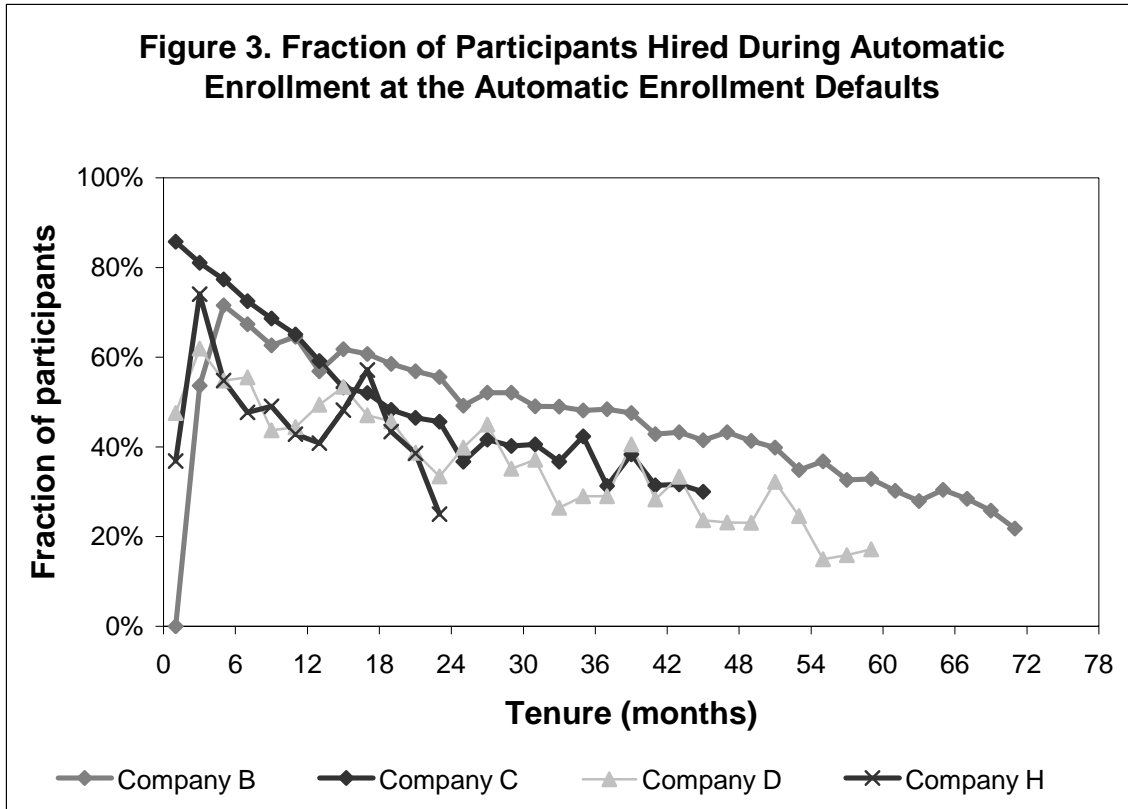
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